



## Michigan's Electricity Market

Michigan House Energy and Technology Committee  
May 14, 2013

**Rod Williamson**, Dow Corning  
Chairman of ABATE

**Rick Coy**, Clark Hill  
ABATE Legal Counsel



### ABATE's Purpose

To represent the industrial viewpoint on energy and utility issues before all appropriate governmental bodies and other pertinent organizations which affect energy pricing, reliability and terms and conditions of service in Michigan.

[www.abate-energy.org](http://www.abate-energy.org)

## Topics Addressed Today

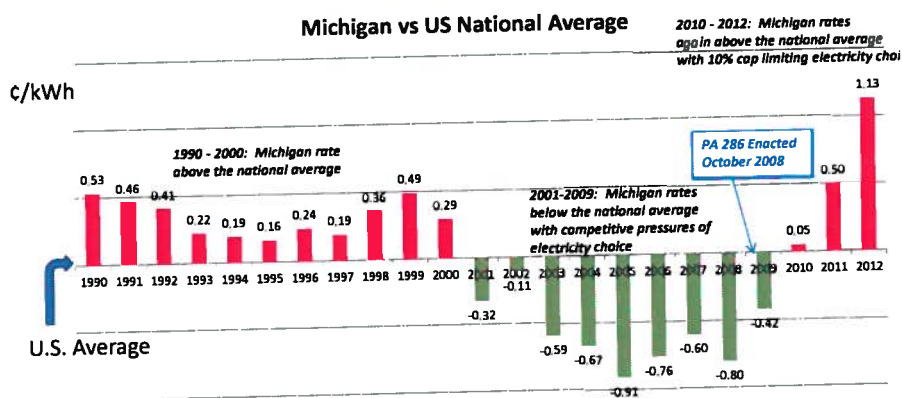
- Rate Impact of Act 286 of 2008
- Competitive Electric Markets
  - Reliability myths
  - Benefits to those who do not choose
- Limiting the cost of environmental mandates
  - Securitization provides huge savings
- Reforms needed to Act 286 of 2008
  - Restore competitive market
  - End self-implemented rates by utilities
  - Set rates on actual, not projected, costs
  - Require competitive procurement of new supplies



3

## What has the 2008 Energy Legislation done?

**Electricity supply competition limited to 10% = no market competition to help control regulated utility cost**



Source: U.S. Energy Information Administration

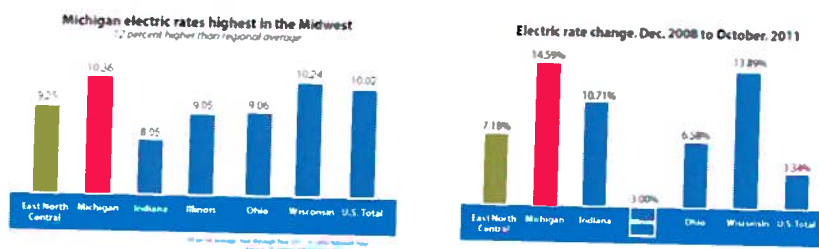
4

All of which has now resulted in:

Michigan's regulated electricity rates being the highest in the mid-west

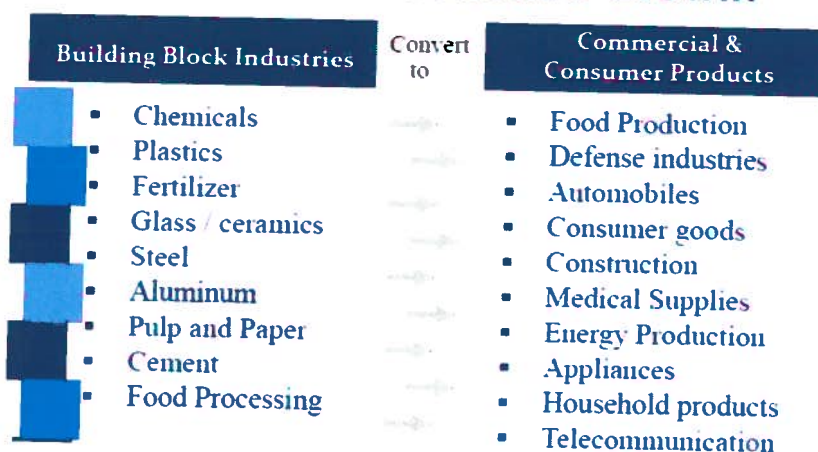
And

increasing at a rate almost 5 times higher than the national average!



5

## Energy Price Sensitive Products are Essential for Economic Growth

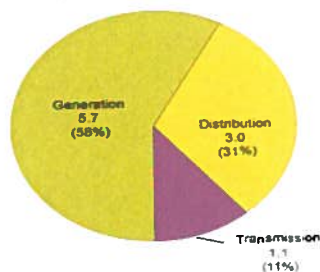


5

## What has the 2008 Energy Legislation done?

In 2008 Michigan: (a) changed the regulatory model where now it has failed to ensure we have competitively priced electricity rates, and (b) LIMITED ANY ALTERNATIVES BY CAPPING the market competition at 10% of a utility's customer purchases of electricity.

**Major Components of U.S. Average Electricity Price, 2011**



Source: U.S. Energy Information Administration, Annual Energy Outlook 2012, Reference Case, Table 8: Electricity Supply, Distribution, Prices, and Emissions

7

## Michigan's Electricity Market

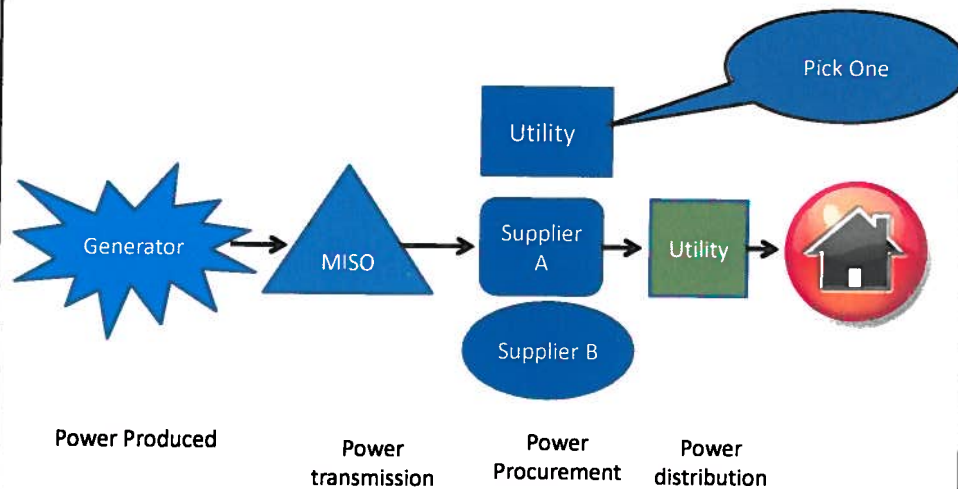
A Path Forward:

Retail Choice



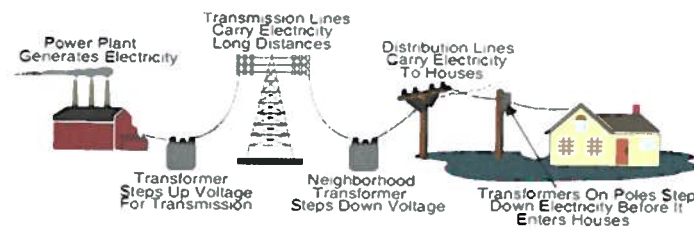
8

## How Power Moves **With** Competition



9

## Reliability



Source: EIA

- In a competitive / retail choice market **nothing changes regarding the delivery** of the electricity. Reliability is maintained by the utilities and transmission companies.
- For generation, each load serving entity must either own or have under contract enough generation to serve customers. In a competitive market, generation will and did get built if there is not enough to meet demand.

10

## Reliability: FACTS on Building Michigan Generation:

### Type of System

- Under Regulation 1990 – 2013

### Results

- Zero (0)

0

- Under Customer Choice 2000 - 2008

- 5 new power plants  
4000 MWs



11

## Reliability Is Not Compromised



- Reliability is always mandatory regardless of type of market
- Industrial customers would not tolerate or accept an unreliable system; their business depends on it
- States with retail choice are not less reliable
- Dr. O'Connor testified: reliability "a false argument"
- Former Commissioners Chappelle and Nelson testified: reliability questions as "misrepresentations and inaccuracies"

12

## Competitive Price

### **Potential Choice Savings for Michigan**

- Market is now \$25/MWh less than utility supply.
- 9.4 million MWh served competitively = 11%.
- 9.4 million MWh in the unserved queue = 11%.
- 9.4 million MWh x \$25 = \$235 million in potential savings.



#### Sources:

- ABATE member average per MWh savings in 2012
- "Status of Electric Competition in Michigan," PSC, February 1, 2013

23

## Competitive Price

### **ABATE Member Experience**

- 2012 Choice savings in Michigan: \$34 million (25% savings)
- 2012 Choice savings in other states compared to average Michigan utility rates: \$65 million



14

## Residential Users Will Share Benefits, Not be Left With Higher Costs

- Residential rates were held down while we had choice
- Explosive growth of residential choice in PA, IL, OH
- Need to make residential aggregation easier
  - By municipality (e.g., Chicago)
  - By, towns, subdivision, or other associations
- 560,000+ MI Residential Customers Choose their Natural Gas Supplier



15

## Residential Users Will Benefit

- A competitive market will hold prices down for all customers
- The cost of power supplies to serve residential customer was held **DOWN** when we had customer choice
- The cost of power supplies to serve residential customers went **UP** when choice was **eliminated** for most in 2008



16



## Does Competition Raise the Cost of Utility Services?????



- Those currently opposing more competition claim so
- This defies logic, common sense, and basic economic principals
- Their theory: If there are more sellers, prices will rise ?!#\$?
  - Reality: More sellers reduce prices
- It also defies the actual experience we had from 2000-2008
  - Competition helped restrain price increases for those who stayed and for those who chose a new supplier

## Simplistic Misrepresentation of Choice Opponents



**Fixed costs**



**Customers**

## Opponents of Choice Want It Assumed:

- All Costs Are Fixed Costs



- But its not true

- Variable costs make up a large portion of utility operating expenses
  - Especially for fuel and purchased power
  - Which are **reduced** when there are fewer customers

**Question at Hand** – *Want an answer, not a conjecture.*

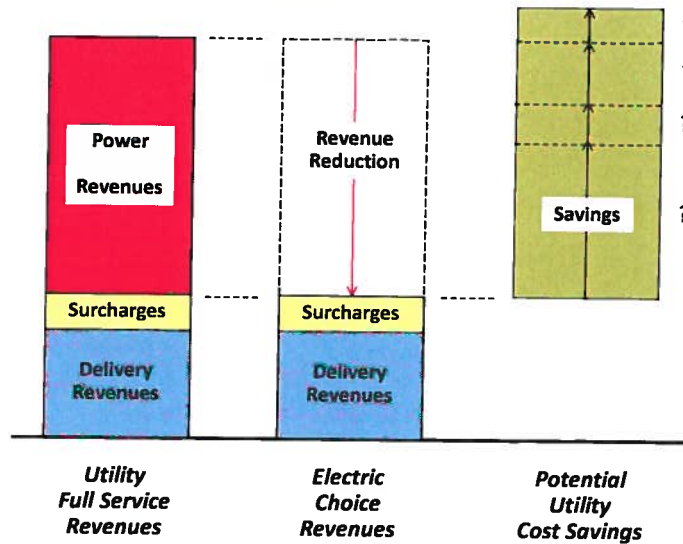
“When customers migrate to Electric Choice, do the remaining Full-Service customers have to pay more to make up the utility’s lost revenue?”

?

MYTHBUSTERS

- |   |                         |
|---|-------------------------|
| • <i>Plausible assertion ?</i>          | • Evidence              |
| • <i>Rhetorical connectivity ?</i>      | • Logic                 |
| • <i>Sound bite – “details at 11” ?</i> | • Meaningful Conclusion |

**Situation** -- *The power supply portion of utility revenues decrease when customers migrate to Electric Choice, but what are the associated cost savings?*



21

### **Types of Power Supply Cost Savings --**

*Potential savings in the PSCR, plus longer-term efficiencies.*

#### **Immediate and Quantifiable Savings Candidates**

- Reductions in Costs**
  - Fuel costs at the margin
  - Wholesale energy purchases
  - Summer capacity purchases
  - Mandated renewable purchases
  - Transmission costs (*AESs pay*)
  - Line loss multiplier on savings (*DE 6.8%, CE 8.6%*)
  - Various Midwest ISO charges

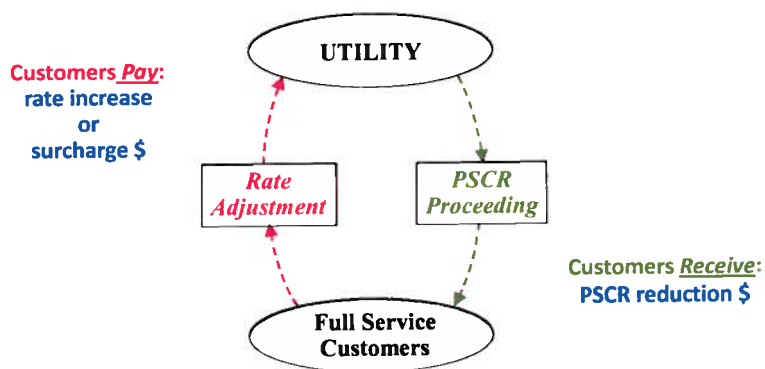
- Increases in Revenues**
  - Wholesale energy sales
  - Sales of ancillary services to Midwest ISO
  - Capacity sales

#### **Longer-Term Efficiencies (additional to following quantification)**

- Improvements in Portfolio Efficiencies**
  - Reduction in generation maintenance expenses (*DE 1.2 ¢*)
  - Optimization of generation portfolio

22

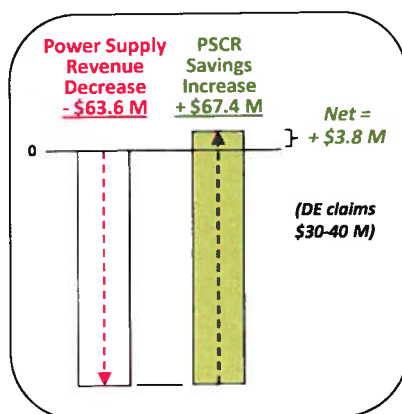
**How Netting Works** – PSCR savings & rate increase/surcharge are netted via two proceedings – not one.  
Customers see little change in net paid.



23

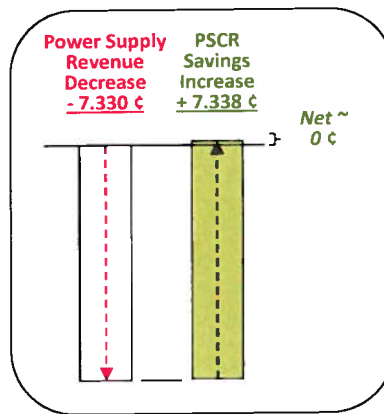
**Results** – From utility data, the savings are very close to the reduction in revenues.

For DE (per 1 million MWh)



Excerpt: Case No U-16472, Exhibit EM-3

For CE (¢ per kWh)



Excerpt: Case No U-16566, Exhibit EM-2

24

## So, Do Not Be Mislead



- Customers who stay, rather than choose a new electric supplier, **SHOULD NOT GET STUCK PAYING MORE** in the real world

25

### Other Benefits of a Competitive Market:

#### **Adaptability**



The competitive market is quick to adjust to changing market conditions. Recently when electricity demand dropped in Michigan due to the recession and new environmental regulations were being put in place impacting coal fired generation, **a competitive supplier** responded and canceled plans to build a coal fired generation facility in Michigan. This change **did not cost customers anything!**

Under the regulated model when **a utility** decided to cancel their plans to build a coal fired generation facility, **customers had to pay over \$14M** to the utility to cover engineering and planning cost.

25

## Michigan's Electricity Market A Path Forward

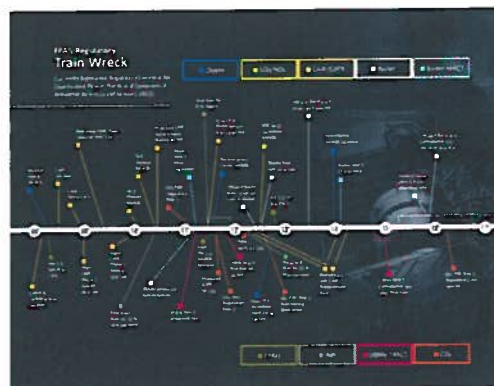


If we do not fully deregulate the market where the utilities no longer own generation and there is full competition for the generation supply...

Then we need several changes to help control the skyrocketing regulated utility rates!

27

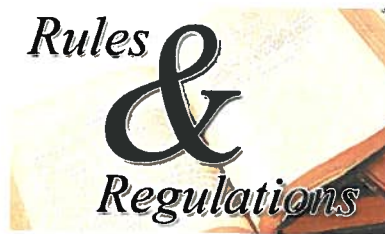
## Securitization: Limiting the Cost Impact of Environmental Mandates



28

## New Regulations

New EPA rules, such as EGU MACT (MATS), Section 316b regulations, coal combustion by-products or residue rules, require electric utilities to invest billions of dollars in water and pollution control facilities or shut down generating plants.



29

## What we know



- Most aspects of the regulations are finalized
- Some costs may be unclear, BUT
  - We know its already here
  - We know the costs are very large
  - We know these are not in the ordinary course of business expenditures, not to increase supply, not to improve reliability, and not to improve customer service

30

## Securitization

- Securitization is the process by which a utility, following the issuance of a financing order by the PSC, substitutes relatively high-cost debt and equity with lower-cost debt in the form of securitization bonds.



- If water and pollution control facilities were financed by securitization bonds instead of traditional financing, then the savings to all customers of the utility are enormous

31

## Estimated Expenditures

### Consumers Energy

- \$1.1 billion

### Detroit Edison

- \$1.8 billion



32



## So what are the savings from Securitization:



### Consumers Energy

- Traditional Ratemaking costs customers \$2.1 billion
- Securitization costs \$.8 billion
- **Savings = \$1.3 billion**

### Detroit Edison

- Traditional Ratemaking costs customers \$4.0 billion
- Securitization costs \$1.6 billion
- **Savings = \$2.4 billion**

33

## Reforms Needed to Act 286



34

## Need to eliminate utility self-implemented rates



35

## Self-Implemented Rates

- Act 286 allows utilities to self-implement rates up to the amount requested 180 days after the filing of the application.
- Since the passage of Act 286 in 2008, utilities have self-implemented over \$1 billion in rate increases.
- No standards govern the rates.
- Prior to Act 286: Utilities had to make a showing that they deserved an interim increase.
- Staff would review finances and issue a report.
- Time value of \$1 billion over 6 months = \$15 million (3% interest rate).



36

## Conclusions cont.

- Need legislation that requires utilities to utilize a competitive bid process which is open to all relevant stakeholders to procure electricity to meet anticipated future demand

43

## Questions



44

## Competitive Procurement Process

- Michigan needs a competitive bid supply planning process that makes planning more open to relevant governmental agencies, consumer groups, and others, thus considering the needs and ideas of all parties with a stake in the future of the electric system.



- This process will ensure that the electricity customers are being protected by allowing the lowest cost option for new electricity supply to be identified.

41

## Conclusions

- Need to eliminate the 10% cap on participation in Michigan's electric choice program
  - Will still have reliable service
  - Residential customers will benefit
- Need legislation that requires utilities to utilize lower cost securitization financing for mandated water and air pollution control equipment
- Need to eliminate utility self-implemented rates
- Utilities need to utilize **ACTUAL COSTS** in rate cases – not **ESTIMATED COSTS WHICH MAY NEVER BE SPENT**

42

## Need a Competitive Procurement Process for New Electricity Supply



39

## Electricity Supply Planning

- Within Michigan's regulated model, the method of electric resource planning has been a fragmented process where individual regulated utilities decide how they want to meet the need for new electricity supply.
- This isolated approach only allows for other key stakeholders and public consultation as a last step, if at all, when plans are virtually complete.
- We have done one time analysis and reports like the 21<sup>st</sup> Century Energy Plan but these quickly become outdated and simply sit on the shelf.

40

**Utilities need to utilize ACTUAL COSTS in rate cases – not ESTIMATED COSTS WHICH MAY NEVER BE SPENT**



37

## Projected Costs vs. Actual Costs

- Act 286 states:  
"A utility may use projected costs and revenues for a future consecutive 12-month period in developing its requested rates and charges."
- "Projected costs" is an unworkable standard.
- Utilities can project investment and then not make that investment.
- The prohibition against retroactive ratemaking prevents the Commission from rescinding a previous rate increase
- "Actual costs" are verifiable and allow for more accurate rates.
- With the ability for the utility to file a new rate case every 12 months, there is no need to use projected costs.



38